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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1961.

No. 544/61.

ARTHUR H. SHAFFER and M. JAMES SPITZER, Trustees, *Petitioners*,

vs.

C. GORDON ANDERSON, As Trustee in Reorganization, *Respondent*.

BRIEF OF RESPONDENT IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

HARRY N. BOUREAU,
of
SHUTTS, BOWEN, SIMMONS, PREVATT & BOUREAU,
1010 First National Bank Building,
Miami 32, Florida,
Attorney for Respondent.

E. L. MENDENHALL, INC., 1108 Oak Street, Kansas City 6, Mo., HArrison 1-3030

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STATEMENT OF THE CASE.

Petitioners' complaint to the Court of Appeals and now to this Court is that they were not permitted by the District Court to consummate a plan of reorganization of the debtor (TMT) which placed the entire control of the debtor in their hands. (138-160)* They were to receive all of the 500,000

*References are to pages of the printed record unless otherwise indicated.

shares of common stock to be issued by the reorganized company and this stock carried all the voting rights. They were to receive, in addition, 250,000 shares of convertible preferred stock and certain other assets. Six of the nine members of the Board of Directors of the reorganized company were to be elected by the common stockholders, so petitioners would be able to control the company. Unsecured creditors with claims in excess of three million dollars were to receive 17 1 2% of their claims in preferred stock to be retired out of a portion of the earnings of the company. Certain maritime lien claimants were to receive some cash and preferred stock.

The crux of this case is why this plan was set aside, and the basic fallacy in the argument of petitioners is that they have been harmed or their rights impaired by the setting aside of the plan and by the District Court's order to the trustee to prepare and submit a new plan of reorganization. The truth is that the petitioners have exactly the same rights that they had when the reorganization proceedings began and have lost none of them during the process of preparing and setting aside the initial plan of reorganization.

Petitioners claim that $330,000 principal debt is due them secured by first preferred ship mortgages covering four vessels of the debtor. This was their claim initially and it is their claim today. Their claim has not yet been liquidated as to validity, amount or priority, such issues being presently pending before a special master appointed by the District Court to consider the same and report to the court, along with similar issues with respect to other lien claims. (Pages 18a-19a, Appendix to Petition for Writ of Certiorari herein).

The initial plan of reorganization which turned the debtor over to petitioners had been approved and confirmed over the strenuous objections of the Securities and

Exchange Commission and of a committee representing stockholders (123, 126, 169, 179), and an appeal by the stockholders from the order confirming the plan was heard by the Court of Appeals along with Petitioners' appeal to that court.

When the trustee and petitioners moved to consummate the initial plan of reorganization (212, 213) the SEC objected, alleging among other reasons the need for an adequate investigation under Sec. 167 of the Bankruptcy Act (216-232). The Court ordered the investigation (245-246) and the trustee filed a complete report of its results (255-295). Among the facts disclosed in this report and which caused the trustee to change his mind about the plan of reorganization and to recommend that it be set aside were:

1. Of some four million shares of TMT stock outstanding with the public, nearly half had been marketed through Arthur H. Shaffer (one of the appellants here) or Joseph Abrams, a stock speculator who, at the time of the investigation, was serving time in Federal prison for defrauding the government. (286)

2. Shaffer and Abrams worked together on many of the stock issues, including the marketing of petitioners' mortgage which was a combination stock issue and mortgage loan. All but one of the original participants in this mortgage were obtained through Shaffer or Abrams. (276) Caplan, the original mortgage trustee, was a front for Shaffer (275), and Abrams was represented among the participants by Bostwick-Westbury Corp., which he controlled (277), and by his uncle, Charles Gordon.

3. Shaffer and Abrams knew at the time they raised the money for the mortgage that TMT was in precarious financial difficulty. (272-273) The loan was made only four weeks before the involuntary reorganization petition

was filed. Therefore, the security demanded was a first preferred mortgage on the ships which were at the time the only source of revenue for the company, and the terms of the loan were harsh—a loan payable in full within 7 months with a $49,500 bonus which amounted to a 15% discount on the face amount of $330,000. (275)

4. Shaffer and Abrams had made large profits from the sale of unregistered TMT stock which they had obtained through their close connection with the management of the company and which they sold to the public although they had obtained all of it under circumstances by which, under the securities laws, it should have been held for investment purposes. (281) In the case of Shaffer, the profits were made by his wife since the transactions were made in her name though arranged by Shaffer. (281)

These were among the facts disclosed by the investigation which led the trustee to conclude that it would not be fair and equitable to turn the debtor over to the mortgage group represented by petitioners and to so recommend to the court.

When the trustee's Report of Investigation came on for hearing, only petitioners opposed the setting aside of the plan of reorganization, although a synopsis of the report, including the recommendations was ordered sent to all creditors and stockholders. (296) It is true, as stated in petitioners' statement of the facts, that all creditors had accepted or acquiesced in the plan of reorganization, so it is significant that only petitioners among the many creditors opposed the formation of a new plan.

Petitioners' main argument is that this initial plan of reorganization constituted a "settlement" of their claim that cannot be set aside. It was no more a "settlement" of petitioners' claim, however, than it was of all creditors'

claims. This is true because *none* of the more than five million dollars in claims had been liquidated prior to the confirmation of this plan of reorganization. The Order Approving the Plan of Reorganization (135) appointed a special master to consider the trustee's objections to claims. (137) All major claims against the debtor were dealt with in the plan and were "settled" *but only for the purposes of such plan.* When the plan was set aside the rights of all creditors as well as stockholders reverted to their former status as claimants, with none of those rights impaired.

No rights were impaired, including those of petitioners, because *no steps whatever had been taken toward consummating the reorganization plan.* No assets had been turned over to the reorganized company; none of the new capital stock had been issued; none of the claimants had been paid in whole or in part; none of the documents executed (or even prepared) which were required to consummate the plan. None of the steps toward consummating the plan had or have been taken as specified in Sec. 229 of the Bankruptcy Act. (Page 16a-17a of Appendix to the Petition herein)

The trustee continues to operate the business of the debtor in a highly successful manner. The latest figures in the printed record show that the total earned surplus under the trusteeship was $576,904.00 as of October 31, 1960 (428), after depreciation, representing less than 3 years operations, for an average of better than $200,000 profit each year. (There are no federal income taxes to pay because of loss carryovers from previous years.) These earnings have been made after paying heavy reorganization expenses not attributable to normal operations. Subsequent to the figures, the record in the District Court shows earnings at even higher rates.

It is the position of the trustee that the rights of none of the interested parties have been impaired by the setting aside of the initial plan of reorganization, that equity and justice require that he be permitted to prepare and present a new plan. If petitioners' claim is as good as alleged, it will have to be accorded appropriate treatment in the new plan, and all of petitioners' rights will have to be protected in the manner required by law.

ARGUMENT.

It is the position of respondent that there exist no special or important reasons for review by this Court of the decision of the Court of Appeals, that petitioners have had a complete review of the alleged errors of the District Court, that the opinion of the Court of Appeals is an equitable and proper one which requires no review by this Court, that the reorganization proceedings involving TMT are still pending in the District Court with no rights of petitioners impaired, and that any further review by this Court at this time is premature.

We will answer, in order, each of the five reasons advanced by opposing counsel as to why the writ of certiorari should be allowed.

1. There Is No Conflict with Decisions in Other Circuits Regarding the Power to Set Aside a Confirmed but Unconsummated Plan of Reorganization under Sec. 229 of the Bankruptcy Act.

In re Inland Gas Corporation, 275 F.2d 509 (Sixth Circuit, 1960), involved post-confirmation proposals for alteration and modification of the plan proffered under Section 222 of the Bankruptcy Act which vests a certain amount of discretion in the District Court and has been

construed to impose certain standards on such proposals in terms of "congruency" with the confirmed Plan, "material" change of circumstances, etc. In *Inland*, the District Judge exercised his discretion against the new proposals and he and the majority of the Court of Appeals held that those standards had not been met.

In the TMT case, the District Judge did not set aside the confirmed Plan because of proposed *modifications* or *alterations* under Section 222—he scrapped the entirety of the confirmed Plan in an exercise of his inherent equitable power sitting in bankruptcy. The old Plan had been approved, accepted by creditors and confirmed on the basis of inadequate knowledge and in the face of a failure to comply with required statutory procedures. *Inland* has nothing to do with Sec. 229 of the Bankruptcy Act.

Likewise, *Knight* v. *Wertheim & Co.*, 158 F.2d 838 (Second Circuit, 1946), refers only to procedure under Secs. 222 and 223 and not to the setting aside of an entire plan and the formation of a new one.

Country Life Apartments v. *Buckley*, 145 F.2d 935 (Second Circuit, 1944), involved consideration of a pending plan of reorganization and whether it should be materially modified. It did not concern the complete setting aside of the pending plan and the proposed formation of another for the benefit of all interested parties.

In re Diversity Bldg. Corporation, 141 F.2d 65 (Seventh Circuit, 1944), was an attempt to modify a plan of reorganization almost eight years after it had been confirmed and in operation under the court's supervision.

Rights in a confirmed plan "vest" only when it is "substantially consummated" and Sec. 229 sets forth when "substantial consummation" shall be deemed to have taken place. Section 229 expressly precludes material alteration

or modification under Sec. 222 after substantial consummation (as a matter of legislative history, Section 229 is interrelated with Section 222) and its relevance to this case is the inference that, if a plan can be materially altered or modified prior to substantial consummation, *a fortiori*, it can be set aside under circumstances which normally permit a District Court to vacate a non-final order.

None of the cases cited by petitioners limit, or imply any limitation on, the general power of the court to revise non-final orders on the basis of newly discovered evidence or mistake.

2. There Is No Conflict with Other Decisions by the Holding Below That There Can Be No Compromise Settlement of a Claim until After Substantial Consummation of a Plan of Reorganization.

Three cases are cited for the second reason relied on by petitioner for allowance of the writ. The last two are not in point and do not involve an approved plan of reorganization. *Hanssen* v. *Winogren*, 121 F.2d 1011 (Tenth Circuit, 1941), involved a plan of reorganization *which had been consummated in part* so that creditors' rights had become vested and not subject to change.

3. There Is No Conflict in the Decision Below with Decisions of This Court.

Petitioners' argument under their third point is based on the false assumption that they lost some vested rights when the plan of reorganization was set aside. The record shows clearly, as the Court of Appeals found, that no steps whatever had been taken toward consummating the plan. Therefore no intervening rights had accrued. Petitioners have today every right they had at the begin-

ning of the reorganization proceedings. They can acquire no vested rights in any plan of reorganization until some steps have been taken toward consummation.

> "The entire process of rehabilitation, reorganization or liquidation is open to re-examination out of time by the District Court, in its discretion, and subject to intervening rights." *Pfister* v. *Northern Illinois Finance Corp.* 317 U.S. 144, 152.

4. The District Court's Order Vacating the Plain of Reorganization Was Entered After Hearing on Notice to All Parties in Interest.

The Trustee's Report of Investigation was filed July 1, 1960 (255), and the court ordered a hearing to be held on July 14th "to consider and determine what action shall be taken in regard to the recommendations made by the trustee in said report" and a synopsis of the report including the recommendations was ordered sent to all creditors and stockholders. (296) The Trustee notified all creditors and stockholders of the hearing, sent them the synopsis of the Trustee's Report, the court's order for the hearing. The notice as well as the court order stated that the purpose of the hearing was to consider what action should be taken on the Trustee's Report.

The hearing on July 14, 1960, was attended by representatives of all major creditors, the Stockholders Committee, the SEC and the Department of Justice representing the United States as a creditor.

Counsel for petitioners opposed the Trustee's recommendations but their reasons were based solely on certain legal conclusions of the Trustee with respect to the evidence outlined in the Trustee's Report; they did not point out any particular instance wherein the Trustee was not accurate with respect to the facts disclosed by the

investigation and mentioned in the Report. (298-304) This answer only controverts the legal sufficiency of the facts to justify the recommendations made.

Petitioners were the only parties to oppose the trustee's recommendations, and under these circumstances the District Court entered its Preliminary Order (307) and later its final order adopting the trustee's recommendations. (324) Both the District Court and the Appellate Court found that there was good cause shown for the action taken.

Again we emphasize that petitioners' rights as a creditor have not been impaired, that a new plan of reorganization will be prepared that must accord all parties proper consideration of their rights. Petitioners' claim is but a small portion of the total claims involved, and all other parties expressly consented to or acquiesced in the decision that a new plan of reorganization should be prepared.

5. The Decision Below with Respect to Alleged Laches and Estoppel Is Proper and Does Not Conflict with Other Circuit Decisions.

The four cases cited by petitioners in support of their fifth reason why the writ should be allowed do not pertain to situations comparable to the case at bar. The first two relate to compromises of claims that had been carried out in part and in which the claimant could not be restored to his former position. *In re Universal Rubber Products* Co., 25 F.2d 168, involved an effort to recover a sum that had already been paid to a claimant pursuant to an order fixing the amount due. *Nichols* v. *Alker*, 231 F.2d 68, was an effort to attack collaterally a plan of reorganization 18 months after its consummation.

CONCLUSION.

This cause is pending before the District Court on order to the trustee to prepare and submit a new plan of reorganization. Petitioners acquired no vested rights in the initial plan because it was set aside before any steps toward consummation had been taken; so no substantial rights of petitioners have been impaired.

There exist no special or important reasons for another review by this court of the decision of the District Court.

The Petition for Writ of Certiorari should therefore be denied.

Respectfully submitted,

HARRY N. BOUREAU,

of

SHUTTS, BOWEN, SIMMONS, PREVATT & BOUREAU,
1010 First National Bank Building,
Miami 32, Florida.

Attorney for Respondent.

Dated December 11, 1961.